No. 94-1033

IN THE

Supreme Court of the United States

October Term, 1994

COMPUTER CURRICULUM CORPORATION,

Petitioner,

v.

INSTRUCTIONAL SYSTEMS, INC.,
and
DEBORAH T. PORITZ, ATTORNEY GENERAL
OF THE STATE OF NEW JERSEY,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF OF COMPUTING TECHNOLOGY INDUSTRY ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

WILLIAM J. WENZEL
Counsel of Record
PULLMAN & COMLEY
850 Main Street
Bridgeport, CT 06601-7006
(203) 330-2000

January 17, 1995

MOTION OF COMPUTING TECHNOLOGY INDUSTRY ASSOCIATION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE*

The Computing Technology Industry Association ("CompTIA" or "Association") respectfully moves this Court for leave to file the attached brief *amicus curiae* in support of the petition for writ of *certiorari*. The consent of the petitioner has been obtained.* The consent of respondent Instructional Systems, Inc. has been refused. The consent of respondent Deborah T. Poritz, Attorney General of the State of New Jersey, has been sought but has not been granted.

CompTIA is a national not-for-profit association of more than 6,100 microcomputer distributors, manufacturers, resellers, software publishers, and service companies. Its mission is to foster high levels of professional competence and business ethics among its members and throughout the computer industry. Combined sales of member companies reached $50.5 billion in 1993. Total industry-wide microcomputer sales in 1993 in the United States were estimated at $81.7 billion.

The Association's members have a vital interest in the instant case. The Third Circuit's decision poses a significant threat to the ability of suppliers and distributors in the computer industry to decide for themselves the terms on which they will do business throughout the Northeast region and even the entire country.

The practical implications of the decision below for the multibillion-dollar microcomputer industry are enormous.

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* The letter reflecting such consent to the submission of this brief has been filed with the Clerk of the Court.

CompTIA is well situated to assist the Court by alerting it to the practical dangers of extraterritorial application of statutes like the New Jersey Franchise Practices Act. The Association therefore respectfully moves this Court for leave to file the attached brief *amicus curiae*.

Respectfully submitted,

William J. Wenzel
Counsel of Record
PULLMAN & COMLEY
850 Main Street
Bridgeport, CT 06601-7006
(203) 330-2000

January 17, 1995

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INTEREST OF *AMICUS CURIAE*

Amicus curiae the Computing Technology Industry Association ("CompTIA" or "Association") submits this brief in support of the petition for writ of *certiorari*. As discussed in the accompanying motion for leave to file, the Association and its more than 6,100 members have a vital interest in this case.

INTRODUCTION AND SUMMARY OF ARGUMENT

This Court has always stressed that the touchstone of dormant Commerce Clause analysis is a law's "practical effect." *E.g.*, *Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. 573, 583 (1986). The practical effect of the New Jersey Franchise Practices Act, N.J. Stat. Ann. § 56:10-1, *et seq.* ("NJFPA"), as authoritatively construed by the New Jersey Supreme Court, is to disrupt commerce wholly outside New Jersey. Any distribution arrangement with a New Jersey-based distributor is now at risk of being subject to the draconian provisions of the NJFPA even insofar as it relates to *other* States. If the Court of Appeals' decision is permitted to stand, manufacturers that have retained New Jersey-based distributors may find that they are forbidden from changing their method of distribution — in perpetuity — not only in New Jersey, but throughout an entire region or (if the agreement was a nationwide one, which is not uncommon) throughout the entire country.

Moreover, although most States, as well as Congress, have refused to adopt franchise protection statutes for fear of their anti-competitive impact, New Jersey is not the only State with such a law. Several other States — including Wisconsin, Illinois, and Iowa — have similar statutes compelling renewal of franchise or dealership arrangements absent good cause for nonrenewal. The decision below would permit these States, as well as others, to

project their laws extraterritorially in order to rewrite private contracts between distributors and suppliers. Individual States could interfere with interstate commerce on a regional or even national basis.

There are further reasons that this case is of special concern to the computer industry. The New Jersey Supreme Court made clear that agreements between computer manufacturers and distributors are a vulnerable target of franchise termination statutes. The court singled out the close relationship between computing technology suppliers and distributors as exhibiting the "hallmark of the franchise relationship" regulated by the NJFPA. Pet. App. 128a (citation omitted).

Yet there is probably no industry in which it is more important to avoid freezing companies into particular distribution methods by statute. Many hardware and software products on the market today could not have been foreseen only a few years ago. Trends in consumer needs and tastes are equally unpredictable. Accordingly, distribution arrangements — particularly multistate arrangements, which are quite common in the computer industry — must remain flexible. Indeed, modes of distribution in the computer industry are themselves the subjects of rapid change, as lines blur among distributors, franchisors, and franchisees. Market forces are stimulating the development of diverse and innovative methods of distribution on a nationwide basis.

It would be unthinkable to attempt legislatively to freeze business relationships as they exist today. But the NJFPA purports in effect to do just that, by ignoring the parties' own negotiated agreements and bestowing franchises that are by law potentially infinite in duration. The NJFPA does so extraterritorially, on a regional or even nationwide basis.

Hence, respondent ISI's claim in its opposition that "[t]his case has no significance to anyone except ISI and CCC," Opp. Cert. at 15 (quoting argument heading), is completely false. The entire multibillion-dollar computer industry has a vital interest in this case. Other industries do as well, since the scope of the NJFPA and the logic of the decision below cannot be confined to computing technology. Indeed, even distributors have a stake in reversing the decision below: the NJFPA's interference with interstate commerce may work to ISI's benefit in this particular dispute, but it does not advance the interests of distributors overall. If a supplier cannot ensure that a State will honor the supplier's freely negotiated contracts with distributors, it will demand a "risk premium" — such as a higher price — to compensate for the uncertainty it faces, or simply forgo entering into what otherwise might be a mutually advantageous business relationship. Accordingly, leading distributors within the Association voted to file this brief urging this Court to grant the petition for *certiorari*, even though distributors are ostensibly beneficiaries of the New Jersey statute.

REASONS FOR GRANTING THE WRIT

This Court has repeatedly stressed that the dormant Commerce Clause is concerned with, above all else, the *practical effect* of a state law. In the context both of *per se* unlawful extraterritorial laws and of burdens on commerce governed by *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970), "the critical consideration is the overall effect of the statute on both local and interstate activity." *Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. 573, 579 (1986). A law is *per se* invalid if its "practical effect" is "to control [commerce] in other States." *Id.* at 583; *see Healy v. The Beer Institute*, 491 U.S. 324, 336 (1989) ("[t]he critical inquiry is whether the practical effect of the regulation is to control conduct beyond the boundaries of the State"); *Southern Pacific Co. v. Arizona ex rel. Sullivan*, 325 U.S. 761, 775 (1945)

(invalidating law whose "practical effect . . . is to control [conduct] beyond the boundaries of the state").[1]

The practical effect of the NJFPA is to disrupt interstate commerce by regulating, and potentially prohibiting, transactions wholly outside New Jersey. According to the decision below, for example, a manufacturer doing business with a New Jersey distributor could be enjoined, in perpetuity, from changing its methods of distribution in other States. This would be true even if the goods never pass through New Jersey.

If other States were to follow New Jersey's example of projecting state law extraterritorially to nullify contracts among manufacturers, distributors, and resellers, "the free movement of [goods] in the stream of commerce will be severely impaired" — a process that could "result in the type of balkanization the Clause is primarily intended to prevent." *C&A Carbone, Inc. v. Town of Clarkstown*, 114 S. Ct. 1677, 1690 (1994). "This kind of potential regional and even national regulation" of distribution activities "is reserved by the Commerce Clause to the Federal Government and may not be accomplished piecemeal through the extraterritorial reach of individual state statutes." *Healy*, 491 U.S. at 340.

This threat is not hypothetical. Some eighteen other States have adopted franchise termination statutes,[2] although most are not as

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[1] *See also C&A Carbone, Inc. v. Town of Clarkstown*, 114 S. Ct. 1677, 1684 (1994); *Wyoming v. Oklahoma*, 112 S. Ct. 789, 791 (1992); *Trinova Corp. v. Michigan Dept. of Treasury*, 498 U.S. 358, 372 (1991); *Goldberg v. Sweet*, 488 U.S. 252, 260 (1989); *Lewis v. B.T. Inv. Mgrs., Inc.*, 447 U.S. 27, 37 (1980).

[2] *See* Ark. Code Ann. § 4-72-204; Cal. Bus. & Prof. Code § 20020; Conn. Gen. Stat. Ann. § 42-133f(a); Del. Code Ann. tit. 6, § 2552; D.C. Code. Ann. § 29-1203; Haw. Rev. Stat. § 482E-6; Ill. Rev. Stat. ch. 815, ¶ 705, § 19 & ¶ 710, § 9; Ind. Code Ann. § 23-2-2.7-1; Iowa Code Ann. §§ 523H.1-523H.17; Mich. Comp. Laws Ann. § 445.1527; Minn. Stat. Ann. § 80C.14; Miss. Code Ann. § 75-24-53; Mo. Ann. Stat. § 407.405; Neb. Rev. Stat. § 87-404; N.J. Stat. § 56:10-15; P.R. Laws Ann. tit 14, § 278a;

onerous as the NJFPA.[3] Under the decision below, all of these statutes could be projected extraterritorially, producing a crazy-quilt pattern of state regulation that the Commerce Clause was surely intended to prevent. A supplier's only recourse would be to avoid entering into distribution arrangements with companies based in New Jersey and other States with similar laws. But forcing suppliers to protect themselves by forgoing otherwise profitable business opportunities is itself inefficient and would have a significantly anti-competitive effect on the delivery of goods into other States. In the end, suppliers, distributors, and consumers — even consumers who do not live in States that have such laws — would all be harmed. Moreover, for those suppliers that have existing relationships with distributors located in New Jersey or States with comparable laws, it may already be too late.

The multibillion-dollar computer industry, which is expected to play an increasingly vital role in the national economy in the coming years, is particularly vulnerable to such extraterritorial regulation. Most distributors operate on a multistate basis, serving many dealers throughout the United States. This interstate activity creates the danger that States like New Jersey would be able to justify applying their franchise termination statutes extraterritorially to multistate contracts involving distributors doing business within the

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Tenn. Code Ann. §§ 47-25-1503 to 1504; Va. Code Ann. § 13.1-564; V.I. Code Ann. tit. 12a, § 132; Wash. Rev. Code Ann. § 19.100.180; Wis. Stat. Ann. § 135.03.

[3] Seven of these States distinguish between termination and renewal — allowing non-renewal of franchise agreements with no "good cause" requirement — or require merely that notice be given prior to non-renewal or termination. *See* Cal. Bus. & Prof. Code § 20020; Mich. Comp. Laws Ann. § 445.1527; Minn. Stat. Ann. § 80C.14(3)-(4); Miss. Code Ann. § 75-24-53; Mo. Ann. Stat. § 407.405; Va. Code Ann. § 13.1-564; Wash. Rev. Code Ann. § 19.100.180(2)(i)-(j); *see also* Ind. Code Ann. § 23-2-2.7-1 (requiring good cause for non-renewal but also providing that statute "shall not prohibit a franchise agreement from providing that the agreement is not renewable upon expiration"); Neb. Rev. Stat. § 87-404 (same).

State. Indeed, the New Jersey Supreme Court asserted that, "[b]ecause of the extraordinary and intricate relations that arise in the distribution of computer products, a 'close symbiotic relationship' arises almost of necessity between manufacturers and distributors or resellers." Pet. App. 127a-128a. According to the New Jersey court, such a "symbiotic relationship" between suppliers and distributors is the "hallmark of the franchise relationship," *id.* at 128a (internal quotation omitted) — leading the court to "adapt" legislation enacted on the model of a typical fast-food franchise "to the rapidly-evolving complexities of the computer industry and its various distribution channels." *Id.* at 85a.

Yet the kind of extraterritorial regulation upheld by the Third Circuit would severely disrupt the highly dynamic computer industry. The NJFPA would freeze existing distribution arrangements in place and would strip computer manufacturers, distributors, resellers, and other companies of the flexibility they need to adapt to market changes. Manufacturers, which are often forced (particularly in the early stages of a product's life cycle) to enter into exclusive distribution arrangements, could find themselves bound to one distributor potentially in perpetuity.

This extraterritorial, legislatively enforced rigidity would be disastrous for the computer industry. As a leading industry consultant has observed, "the reseller channel is continually in flux":

> The reality of today's computer industry is that three months can make a liar out of anyone. One bad quarter can send a company's stock and management into the cellar. . . . We have to make intelligent statements about products we have read about but that don't really exist yet. We must make strategic decisions for many consumers that are no more than a wing and a prayer, plus some new technology that will be available in the next quarter.

Susan Spiner, *The Reseller Saga Continues: Crystal Ball Gazing for '94 — the Market Comes Full Circle*, Computing Channels 14 (Dec. 1993). Another commentator has written that "[e]ven the casual observer quickly realizes that constant change is perhaps the only generalization possible regarding distribution channels for computer products." Miles R. Gilburne, *The Granting of Marketing Rights Early in the Product Life Cycle of Hardware and Software: The Problem of Distribution Channel Lock-In*, Computer Lawyer 28 (Feb. 1994). "Given the fragility of distribution practices which may exist at any given time in the computer industry, it is not possible to predict with any certainty what distribution practices will be desirable in even the relatively near term." *Id.* at 32. Accordingly, distribution arrangements "must be structured in such a manner as to maximize future flexibility in what is likely to be an extremely fluid market." *Id.*

The dynamic nature of distribution arrangements in the computer industry is underscored by recent developments blurring the lines among the traditional market roles. For example, the industry's second largest distributor, Merisel, recently acquired a franchisor organization, Computerland, and now plays a dual role in the market. Other franchisors are finding that they can no longer thrive simply as name brand product suppliers. To expand their business, many have added services traditionally offered only by distributors, like lending money to franchisees to finance inventory. Large-format retailers like computer superstores, office product superstores, and warehouse membership clubs, are now viable independent avenues of distribution. Direct sales by manufacturers similarly avoid traditional distribution channels altogether.

Perhaps the most dramatic development is the increasing availability of the computer modem, which enables software companies to disseminate their products electronically to consumers, without the need for the physical transport and delivery of goods that historically have characterized distribution activities. Under

the decision below, however, a supplier with a contractual relationship with a traditional distributor might be inhibited from using the modem to distribute software cheaply and efficiently to consumers — even if the parties expressly preserved in their contract the supplier's right to alter distribution methods in response to market forces and technological change.

In short, the computer industry is changing and consolidating, both technologically and organizationally. Creative approaches are a necessity in the high-volume, low-margin business of distributing small quantities of goods frequently to many different small customers. Any legislative attempt to interfere with the private decisions of companies in the marketplace will hamper efficiency and ultimately injure consumers. Even distributors — the ostensible beneficiaries of franchise termination statutes like the NJFPA — will be harmed, as manufacturers will simply forgo entering into relationships with them or will demand higher prices to compensate the manufacturers for the risk that they might unwittingly become locked into existing distributor channels.

For all these reasons, the extraterritorial state regulation upheld by the Third Circuit threatens to distort dramatically the interstate distribution of goods and services in the computer industry and to disrupt severely commerce occurring wholly outside New Jersey.

CONCLUSION

The petition for writ of *certiorari* should be granted.

Respectfully submitted,

William J. Wenzel
Counsel of Record
PULLMAN & COMLEY
50 Main Street
Bridgeport, CT 06601-7006
(203) 330-2000

January 17, 1995